



MAY 2010

# HONG KONG PRIME OFFICE

Monthly Report

**Knight Frank 萊坊**

## YIELDS SET TO RISE

Over the past month, Hong Kong's office sales market started to consolidate, following a strong period of recovery that started in the second quarter of 2009. The correction was triggered by a number of factors including the recent volatility in global stock markets; the worsening of the European debt crisis; negative impact from tightening measures on the Mainland as well as buyers' resistance to prices which had surged over 75% in the previous 13 months.

Grade-A office prices recorded a 2.7% fall in April—the largest month-on-month decline since February 2009. Price dips were seen in all major Grade-A office districts during the month. Admiralty and Sheung Wan fared the worst, with prices declining 3.5% and 3.3% after surging over 85.7% and 89.3%, respectively. Tsim Sha Tsui also saw prices edge down 3.2%. Grade-A office prices slipped a further 1.5% in May.



Investment sentiment soured after the Labour Day, depressing office sales activity. Sales slowed notably after an active April, as buyers became increasingly cautious. Deals involved mainly small floor plates during the month, such as a 1,820-sq-ft unit in Lippo Centre in Admiralty sold for HK\$28.6 million or HK\$15,700 per sq ft, and a mid-floor unit in East Point Centre in Causeway Bay sold for HK\$16.6 million or HK\$12,500 per sq ft.

While the sales market weakened, the leasing sector remained active, particularly in non-core business areas. The substantial space vacated by an insurance giant in The Lee Gardens in Causeway Bay has been filled quickly, thanks to the revival of corporate expansion activity. Shinewing, a Mainland accounting firm, leased a whole floor in The Lee Gardens last month, while Burberry moved into the same building, vacating their previous space in Convention Plaza Office Tower in Wan Chai. Currently, there are no whole floors available for lease in The Lee Gardens.

Vacant space in Kowloon East also decreased rapidly over the past month, as the district continued to see major leasing deals. Nike committed to three floors with a total area of about 79,000 sq ft in Exchange Tower in Kowloon Bay, while an engineering firm took up 80,000 sq ft of space in Landmark East in Kwun Tong. Some major office buildings have already achieved full occupancy, including Exchange Tower and Manhattan Place in Kowloon Bay as well as Tower One of Landmark East in Kwun Tong. As Kowloon East's vacancy rate has dropped to a single-digit level, leasing activity in the area will slow in the coming months, due to limited availability.

Despite the downward adjustment in office prices, the recovery of office rents showed no signs of abating, with growth accelerating in non-core districts. Notable rent increases of 3.3% and 3.0% were seen in Causeway Bay and Kowloon East respectively, as occupancy improved. Rents in Quarry Bay and Sheung Wan edged up 2.8% and 2.1%, respectively, after remaining stable in March. Central recorded a mild growth of 1.2% in April, after rebounding 18.3% in the previous seven months. The average Grade-A office rents grew a further 1.1% in May after going up 1.4% in April.

Hong Kong's office market cycle has come to the point where rental yields have ceased to decline and are showing signs of a fresh uptrend. Between early 2009 and early 2010, when the office market was in its initial phase of recovery, the average price of Grade-A offices surged more than 70%, far exceeding the average rent growth of 14.6%. During the same period, Grade-A office rental yields plunged from 5.3% to 3.3%, according to the Rating and Valuation Department. This was a phase when property investors priced in a full recovery of the real economy, but the leasing market had yet to catch up. However, as the office sales market enters a consolidation period and leasing demand continues to pick up, yields are set to rise in the coming months.

A big question mark hanging over the market at the moment is whether the sovereign debt crisis in Europe will deepen and spread to other parts of the world. If the crisis worsens, it could give rise to a banking crisis and affect international trade, with the trade credit market being frozen. However, if the crisis in Europe can be contained without seriously affecting the credit market and international trade, leasing demand in Hong Kong's office market should be sustained and rents should continue to rise. This would lay the ground for a fresh upturn in office prices when rental yields claw back to higher levels.



## Prime office report

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Economic indicator	Period	Latest reading	2008	2009	2010 forecast
GDP growth	Q1 2010	+8.2%	+2.4%	-2.7%	+4.5%
Inflation rate	April 2010	+2.4%	+4.3%	+0.5%	+1.5%
Unemployment	Three months to April 2010	4.4%	3.6%	5.4%	4.0%
Prime lending rate	Current	5.00–5.25%	5.3%*	5.0%*	5.0%*

Source: EIU CountryData / Census & Statistics Department / Knight Frank  
# Provisional \* HSBC prime lending rate

Grade-A office prices recorded a 2.7% fall in April—the largest month-on-month decline since February 2009.

District	Net effective rent		Change		Price HK\$psf	Change		
	HK\$psf /mth	From Mar 10	From Jan 10	From Apr 09		From Mar 10	From Jan 10	From Apr 09
Premium Central	129.7	1.0%	10.4%	15.8%	n/a	n/a	n/a	n/a
Traditional Central	83.2	1.4%	5.6%	-2.7%	15,984	-1.0%	7.7%	55.9%
Admiralty	60.8	-0.6%	2.8%	3.8%	13,627	-3.5%	8.7%	61.8%
Sheung Wan	42.2	2.1%	3.4%	4.3%	12,719	-3.3%	6.5%	61.2%
Wan Chai	39.2	1.1%	3.9%	-1.9%	9,954	-0.5%	4.7%	41.2%
Causeway Bay	38.1	3.3%	4.6%	-8.6%	10,074	-1.5%	-0.1%	48.3%
North Point	23.8	2.0%	1.9%	5.6%	n/a	n/a	n/a	n/a
Quarry Bay	33.2	2.8%	3.3%	0.3%	n/a	n/a	n/a	n/a
Tsim Sha Tsui	32.9	1.9%	2.7%	8.0%	9,113	-3.2%	1.8%	44.5%
Cheung Sha Wan	17.0	0.0%	8.4%	17.2%	n/a	n/a	n/a	n/a
Hung Hom	22.2	0.0%	9.8%	17.9%	n/a	n/a	n/a	n/a
Kowloon East	20.1	3.0%	6.2%	16.6%	n/a	n/a	n/a	n/a
Mong Kok / Yau Ma Tei	36.3	0.4%	4.4%	16.5%	n/a	n/a	n/a	n/a

Source: Knight Frank  
Rents and prices are subject to revision.



**Vacant space in Causeway Bay and Kowloon East decreased rapidly over the past month, as the districts continued to see major leasing deals.**

Table 3 Selected office leasing transactions				
District	Building	Tower / floor / unit	Area (sq ft)	Tenant
Causeway Bay	The Lee Gardens	43U/F	17,000	Burberry
Causeway Bay	The Lee Gardens	17/F	15,000	Chopard
Causeway Bay	The Lee Gardens	One floor	16,000	Shinewing
Kowloon Bay	Exchange Tower	9–11/F	80,000	Nike
Kwun Tong	Landmark East	n/a	80,000	An engineering firm
Tsim Sha Tsui	Gateway	One floor	About 20,000	Safilo Group

Source: Knight Frank  
Note: All transactions are subject to confirmation.

**Sales slowed notably after the Labour Day, as buyers became increasingly cautious.**

Table 4 Selected office sales transactions					
District	Building	Floor / unit	Area (sq ft)	Price (HK\$M)	Price (HK\$psf)
Admiralty	Lippo Centre	Tower 2 / mid floor / unit 5	1,820	\$28.6	\$15,700
Causeway Bay	East Point Centre	Mid floor / unit 5	1,324	\$16.6	\$12,500
Admiralty	Lippo Centre	Tower 1 / 10/F / unit 7B	2,050	\$25.5	\$12,430
Sheung Wan	Shun Tak Centre West Wing	18/F / unit 1	2,534	\$30.4	\$11,997
Sheung Wan	Cosco Tower	11/F	19,745	\$217.0	\$10,990
Tsim Sha Tsui	Concordia Plaza	10/F / unit 4	2,526	\$22.8	\$9,026

Source: Economic Property Research Centre / Knight Frank  
Note: All transactions are subject to confirmation.

# RESEARCH



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USA  
Bermuda  
Brazil  
Caribbean  
Australasia  
Australia  
New Zealand

## Europe

UK  
Belgium  
Czech Republic  
France  
Germany  
Hungary  
Ireland  
Italy  
Poland  
Portugal  
Russia  
Spain  
The Netherlands  
Ukraine

## Africa

Botswana  
Kenya  
Malawi  
Nigeria  
South Africa  
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Uganda  
Zambia  
Zimbabwe

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